

Message Text

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PAGE 01 TOKYO 13939 01 OF 02 020910Z
ACTION EA-12

INFO OCT-01 ISO-00 AID-05 CIAE-00 COME-00 EB-08 FRB-01
INR-10 NSAE-00 ICA-20 XMB-04 OPIC-06 SP-02 LAB-04
SIL-01 OMB-01 NSC-05 SS-15 STR-07 CEA-01 EUR-12
PA-02 L-03 /120 W
-----043505 020926Z /14

P 020848Z AUG 78
FM AMEMBASSY TOKYO
TO SECSTATE WASHDC PRIORITY 0092
TREASURY/DEP WASHDC PRIORITY
INFO AMEMBASSY BONN
AMEMBASSY BRUSSELS
AMEMBASSY LONDON
AMEMBASSY PARIS
AMEMBASSY ROME

UNCLAS SECTION 01 OF 02 TOKYO 13939

USEEC

USOECD ALSO FOR EMBASSY

E.O. 11652: N/A
TAGS: EFIN, JA
SUBJECT: FINANCIAL AND ECONOMIC DEVELOPMENTS - JULY 27-
AUG 2

1. SUMMARY: YEN RISE CONTINUES UNABATED TO DISMAY OF
LOCAL OBSERVERS WHO SEE YEN AS BEING PROPELLED BY SPECULA-
TIVE FORCES. TRADING FIRMS EXPORT CONTRACTS TUMBLE IN
JUNE WHILE MITI SURVEY SHOWS SMALL-SCALE EXPORTERS
SQUEEZED HARD AT 200 TO ONE EXCHANGE RATE. MORE CALLS
FOR SUPPLEMENTAL BUDGET IN THE YEN 2 TO 4 TRILLION RANGE
FOLLOW LATEST YEN SURGE. YEN 300 BIL (\$1.6 BIL) TAX
REBATE GOES INTO EFFECT DURING JUNE AND JULY. GUIDELINES
FOR NEXT YEAR'S BUDGET CALL FOR INCREASES IN (MOST)
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PAGE 02 TOKYO 13939 01 OF 02 020910Z

MINISTERIAL BUDGET REQUESTS TO BE LIMITED TO AN AVERAGE
13.8 PCT IN NOMINAL TERMS, A SMALL DECLINE FROM THE
14.6 PCT LIMIT FOR THIS FISCAL YEAR. CALL RATES HAVE
MOVED MORE FREQUENTLY FOLLOWING BOJ LIBERALIZATION MOVE
AND NEW ONE-WEEK MATURITIES IN CALL MARKET TO BE INTRODUCED
IN SEPT. LITTLE CHANGE IN BOND YIELDS IN JULY. OFFICIAL
RESERVES INCREASED \$2,035 BIL IN JULY; INDUSTRIAL PRODUC-

TION DIPPED 0.7 PCT (S.A.) IN JUNE; AND TOKYO CPI CLIMBED 0.8 PCT IN JULY. END SUMMARY.

2. YEN APPRECIATION CONTINUED UNABATED IN THE TOKYO MARKET DURING THE LATEST WEEK WITH THE CURRENCY RISING FROM A CLOSE OF 194.50 ON WED JULY 26 TO A LOW OF 184.30

LATE WED AUG 2. SPOT TRADING VOLUME SOARED TO \$1,123 MIL ON THURS JUL 27, REPORTEDLY THE LARGEST DAILY TURNOVER SINCE AUG 1971, BUT RECEDDED TO LESS FRANTIC LEVELS IN FOLLOWING DAYS. PRESS ACCOUNTS ESTIMATE THAT THE BOJ BOUGHT \$450 MIL ON THURS AND ANOTHER \$200 MIL ON FRIDAY BUT INTERVENTION WAS REPORTED TO BE MINIMAL MON, TUES AND WED AFTER THE YEN HAD MOVED ABOVE 190. COMMERCE DEPT REPORTS THAT THE BILATERAL U.S. PAYMENTS DEFICIT WITH JAPAN HAD INCREASED IN JUNE AND LABOR DEPT REPORTS THAT THE U.S. CPI ROSE AT A 10 PCT ANNUAL RATE DURING JUNE WERE CITED BY MARKET PARTICIPANTS AS FACTORS PROPELLING THE YEN IN RECENT DAYS. DISMAY APPEARS TO BE THE MOST COMMON REACTION TO THE RECENT STRONG YEN SURGE WITH MARKET COMMENTATORS FREQUENTLY VOICING THE OPINION THAT SPECULATIVE FORCES HAVE CARRIED THE RATE BEYOND WHAT CAN BE JUSTIFIED BY UNDERLYING FACTORS. RUMORS THAT FOREX CONTROLS WILL BE TIGHTENED (REPORTED TOKYO 13746) CONTINUE TO CIRCULATE COUPLED WITH STORES THE AUTHORITIES ARE A LITTLE SKITTISH ABOUT TAKING FURTHER STEPS FOR FEAR OF FUELING SPECULATIVE
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PAGE 03 TOKYO 13939 01 OF 02 020910Z

TENDENCIES. AS EVIDENCE OF SUCH BEHAVIOR, MOF OFFICIALS HAVE BEEN QUOTED AS SAYING NON-RESIDENTS FREE YEN ACCOUNTS ROSE BY ABOUT \$1 BIL IN LATE JULY, IN ADDITION TO SUBSTANTIAL LEADS AND LAGS.

3. THE FOREIGN TRADE COUNCIL, AN ORGANIZATION OF 13 MAJOR TRADING FIRMS, REPORTS THAT THE YEN VALUE OF EXPORT CONTRACTS CONCLUDED BY ITS MEMBERS IN JUNE PLUNGED 30.7 PCT FROM ITS YEAR EARLIER LEVEL. IMPORT CONTRACTS, IN CONTRAST, WERE UP 2.3 PCT IN YEN VALUE OVER YEAR EARLIER FIGURES, THE FIRST SUCH INCREASE IN EIGHT MONTHS. METALS AND PLANT EXPORTS WERE REPORTED TO BE DOWN SHARPLY THOUGH AUTO EXPORT CONTRACTS CONTINUED TO RISE. THE FIRMS SURVEYED ACCOUNT FOR ABOUT 60 PCT OF JAPANESE FOREIGN TRADE. SEPARATELY A MITI SURVEY OF SMALL AND MEDIUM-SIZE EXPORTING FIRMS IN 21 REGIONS FOUND THAT, AT A RATE OF 200 TO THE DOLLAR, NONE OF THE FIRMS THOUGHT THEY HAD ANY ELBOW ROOM TO ABSORB FURTHER APPRECIATION AND HALF OF THE FIRMS SURVEYED THOUGHT THEY WOULD BE FORCED OUT OF BUSINESS.

4. THE RISING YEN FLUSHED OUT MORE CALLS FTD SUPPLEMENTARY FISCAL STIMULUS OVER THE LAST WEEK. LDP EXECUTIVE COUNCIL

CHAIRMAN NAKASONE ENTERED THE BIDDING WITH A CALL FOR A YEN 2 TRILLION SUPPLEMENTARY BUDGET. SUBSEQUENTLY, A GROUP OF UNIVERSITY ECONOMISTS SURVEYED BY THE KANSAI ECONOMIC RESEARCH CENTER REPORTEDLY AGREED THE OFFICIAL 7 PCT GROWTH TARGET COULD NOT BE ACHIEVED WITHOUT ADDITIONAL STIMULUS. PROFESSOR MORIGUCHI OF KYOTO UNIV REPORTEDLY URGED A 3 TRILLION YEN SUPPLEMENTAL BUDGET CONCENTRATED ON PUBLIC WORKS SPENDING. OTHERS RECOMMENDED INCOME TAX CUTS IN THE 500 BIL TO 1 TRILLION YEN RANGE AS WELL AS

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PAGE 01 TOKYO 13939 02 OF 02 020917Z

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P 020848Z AUG 78
FM AMEMBASSY TOKYO
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UNCLAS SECTION 02 OF 02 TOKYO 13939

ADDITIONAL PUBLIC SPENDING. NIHON KEIZAI, DRAWING ON ITS NEEDS MODEL, SAID 4 TRILLION YEN OF ADDITIONAL FISCAL STIMULUS WOULD BE NEEDED IN ORDER TO HIT THE 7 PCT TARGET.

5. THI 300 BIL YEN (APPROX \$1.6 BIL) INCOME TAX REBATE PASSED IN THE FY 78 BUDGET WAS IMPLEMENTED DURING JUNE AND JULY. THE REBATE WORKS OUT TO 15,000 YEN (APPROX \$80) FOR AN AVERAGE FAMILY OF FOUR.

6. CABINET MINISTERS APPROVED JULY 28 A 13.8 PCT CEILING IN NOMINAL TERMS ON THE OVERALL INCREASE IN (MOST) MINISTERIAL BUDGET REQUESTS FOR FY 79 STARTING IN APRIL 1979. NEXT YEAR'S BUDGET REQUESTS ARE TO BE SUBMITTED BY END OF AUG. THE CEILING IS A LITTLE LOWER THAN THE

14.6 PCT GROWTH APPROVED FOR SIMILAR REQUESTS FOR CURRENT
FY 78. THE FY 78 BUDGET, AS PASSED IN APRIL THIS YEAR,
AMOUNTED TO 34.3 TRILLION YEN (APPROX \$180 BIL), UP
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PAGE 02 TOKYO 13939 02 OF 02 020917Z

20.3 PCT OVER THE INITIAL BUDGET IN THE PRIOR YEAR.
SEPARATELY MOF ANNOUNCED THAT TAX REVENUES DURING THE JFY
77 HAD RUN A LITTLE ABOVE PROJECTIONS SO THAT THE ACTUAL
DEGREE OF BOND DEPENDENCE LAST YEAR WAS 32.9 PCT RATHER
THAN THE PROJECTED 34 PCT. HOWEVER, FOR THE APRIL-JUNE
QUARTER MOF SPOKESMAN SAID TAX REVENUES WERE RUNNING
BELOW PROJECTIONS BUT THAT IT WAS TOO EARLY TO BE
PESSIMISTIC -- OR OPTIMISTIC -- ABOUT THE LIKELY FULL-YEAR
OUTTURN.

7. CALL MONEY RATES FLUCTUATED MORE FREQUENTLY IN JULY
THAN IN JUNE. CALL RATES WERE CHANGED EIGHT TIMES DURING
THE MONTH (RAISED FIVE TIMES AND LOWERED THREE TIMES)
BRINGING AVERAGE CALL MONEY RATE (JEI 178) FOR JULY UP TO
4.442 PCT PER ANNUM FROM THE 4.106 PCT AVERAGED IN JUNE.
JULY INCREASE APPEARS TO HAVE REFLECTED USUAL SEASONAL
UPSWING. BILL DISCOUNT RATE HAS REMAINED UNCHANGED AT
4.75 PCT PER ANNUM THROUGHOUT THE MONTH. NIHON KEIZAI
DATED JULY 30 REPORTED CALL MONEY MARKET WILL BE LIBER-
ALIZED FURTHER. ACCORDING TO THE PRESS ACCOUNTS, BANK OF
JAPAN INTENDS TO ALLOW CALL LOANS WITH ONE WEEK MATURITIES
BEGINNING IN SEPTEMBER. AT PRESENT, THERE ARE TWO TYPES
OF CALL LOANS, OVERNIGHT DELIVERY AND UNCONDITIONAL WHICH
IS DELIVERED ONE DAY AFTER NOTICE. IN FACT, CALL LOANS
TRADED ON THE MARKET ARE VIRTUALLY ALL UNCONDITIONAL AT
PRESENT. IT IS ALSO REPORTED THE BOJ WILL PERMIT
LIBERALIZED INTEREST RATES ON ONE-WEEK CALL LOANS IN
CONTRAST TO THE PRESENT FIXED RATE PRACTICE ON CALL MONEY
MARKET.

8. SECONDARY MARKET BOND YIELDS REMAINED VIRTUALLY
UNCHANGED IN JULY EXCEPT FOR INDUSTRIAL BONDS. INDUSTRIAL
BOND YIELDS ROSE 0.06 PERCENTAGE POINTS IN JULY, RECORDING
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PAGE 03 TOKYO 13939 02 OF 02 020917Z

THE THIRD STRAIGHT MONTH OF INCREASE.

SECONDARY MARKET BOND YIELDS, END OF MONTH (ANNUAL RATE
IN PCT):

- GOVT BONDS TELEPHONE AND TEL- INDUSTRIAL

- EGRAPH BONDS BONDS

MAY	6.004	6.587	7.100
JUNE	6.065	6.623	7.247
JULY	6.066	6.620	7.308

9. JAPANESE OFFICIAL RESERVES INCREASED BY \$2,035 BIL DURING JULY TO STAND AT \$29,366 BIL AT MONTH END (TOKYO 13836). THE BULK OF THE INCREASE WAS ATTRIBUTED TO FOREIGN EXCHANGE MARKET INTERVENTION DURING THE MONTH.

10. INDUSTRIAL PRODUCTION DIPPED 0.7 PCT (S.A.) IN JUNE WITH ALL-INDUSTRY INDEX NOW STANDING AT 121.5. SHIPMENTS WERE OFF 0.3 PCT (S.A.) AS INVENTORIES CONTINUED TO DECLINE (TOKYO 13492).

11. TOKYO CPI IN JULY ROSE 0.8 PCT (N.S.A.) TO STAND AT 124.6 (TOKYO 13635). MANSFIELD

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